R9050-3A

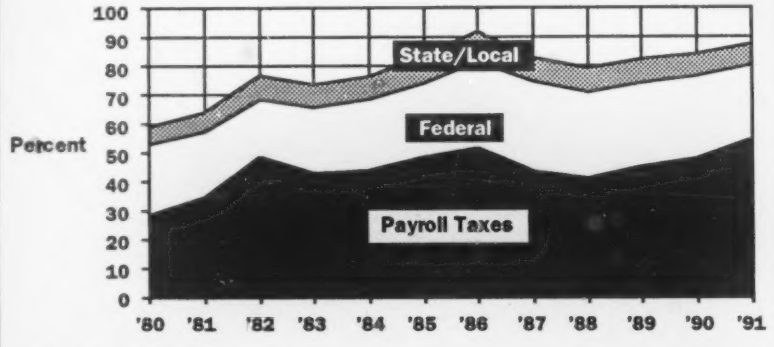
Tax Foundation Vol. 35, No. 6 July 1991

Tax Features

New Study Shows Corporate Taxes Rising Despite Falling Profits

Despite recent declines in corporate profitability, the combined federal, state and local tax burden on American corporations rose steadily

Corporate Income and Payroll Taxes Relative to Corporate Profits 1980-1991



Source: Tax Foundation

State and local corporate income taxes have been increasing rapidly, and corporate payroll taxes are now the largest part of the business tax burden. Over the past decade, the combination of these increases with federal income taxes have caused a sharp rise in the overall corporate tax burden.

from 1980 to 1991, according to a new study by the Tax Foundation. Entitled *Corporate Tax Burden Rises As Profits Fall*, the study asserts that particularly rapid increases which have occurred in payroll taxes and state/local income taxes belie the notion that corporations do not shoulder their "fair share" of the tax load.

A good barometer of the corporate tax burden is a comparison of corporate taxes with corporate profits (see chart above). In 1980, corporate profits made up 10.8 percent of national income but had dived to 6.3 percent by 1990. Total corporate taxes did not experience a comparable decline, so that relative to profits, taxes increased 28.1 percentage points from 58.9 percent in 1980 to an estimated 87.0 percent in 1991. Throughout the 1970s, this rate averaged only 60 percent.

See Corporate Tax Burden on page 2

Tax Foundation

IN THIS ISSUE

Corporate Tax Burden	1
"Front Burner"	1
Luxury Taxes	3
Ways & Means Testimony	6
Government Taxing and Spending	6
Foundation Message	7
Foundation Events	8

FRONT BURNER

Progress on Complicated Art of Tax Simplification

Senator Lloyd Bentsen

Tax simplification can be a complicated process, but it doesn't have to be contentious. A pair of identical bills — S.1394 and H.R. 2777 — show how, working together, we can make progress toward streamlining America's tax laws.

Last month, I joined with House Ways and Means Committee Chairman Dan Rostenkowski, Senator Bob Packwood, the ranking Republican on the Senate Finance Committee, and Congressman Bill Archer, the ranking Republican on Ways and Means, in introducing these identical tax simplification bills.

The tax simplification proposals were developed in consultation with the Democratic and Republican staffs of the Finance Committee and the Ways and Means Committee, and the staffs of the Joint Committee on Taxation, the Treasury Department and the Internal Revenue Service. The staffs were directed to draft tax simplification proposals that, first, did not represent a change in tax policy, and, second, were either revenue neutral or had only a minimal revenue impact.

The tax simplification bill is not intended to be a completed project. It does not represent the final word on how the tax code can and should be simplified. Rather, the legislation is intended to start a dialogue on tax simplification proposals, to put some legislative language on the table. That way Americans will be able to take a closer look at the details of these proposals and obtain a better idea about how

See Bentsen on page 2

Senator Lloyd Bentsen, Democrat from Texas, is Chairman of the Senate Finance Committee.

The opinions expressed in the Front Burner are not necessarily those of the Tax Foundation. Editorial replies are encouraged.

Bentsen from page 1

they would work. The resulting comments and suggestions from taxpayers and tax practitioners will help us further refine these proposals when necessary.

As Chairman of the Senate Finance Committee, I will also be scheduling hearings on the legislation and tax simplification proposals more generally. I very much hope that the introduction of this bill will stimulate serious thinking and comment on how we can make our tax laws more simple.

"The bill provides for a simplified form for individual tax returns. It would also simplify the reporting requirements for partnerships."

Because of budgetary considerations, this bill represents a limited effort to simplify the tax rules. It is extremely difficult and perhaps impossible to enact major structural simplifications to the tax system without encountering serious revenue problems. We are severely constrained in this effort by the pay-as-you-go rules, and I will not move this bill or any part of the bill through the Finance Committee unless it pays for itself.

Even within the constraints the staffs operated under, our legislation includes a number of significant provisions. The bill provides for a simplified form for individual tax returns. It would also simplify the reporting requirements for partnerships. And it would significantly simplify the look-back method for calculating income from long-term contracts. These and other areas in the tax code have tied taxpayers and practitioners in knots and are ripe for simplification. In addition, the bill would enable the Internal Revenue Service to accept tax payments by credit card and thus simplify the payment of taxes once the tax forms have been filled out.

Two important areas in which we were unable to include proposals at this point were payroll tax deposit reform and simplification of the earned income tax credit. Simplification is seriously needed in both areas —no doubt about it. While we were unable to reach agreement on the details of proposals in these areas to include in this bill, we will want to take a further look at these and other proposals as the tax simplification bill advances through the legislative process.

This bill represents one of a series of initiatives to simplify the tax laws. In the area of pension law, Senator David Pryor, Chairman of the Finance Subcommittee on Private Retirement Plans, and I introduced the Employee Benefits Simplification and Expansion Act of 1991 to encourage pension plans for more American workers. By streamlining the cumbersome pension laws, that legislation would encourage more employers to establish pension plan coverage for their employees.

The tax simplification legislation now on the table is an important first step. As we move forward, I'll be interested in hearing what American taxpayers and the people who must deal with the tax laws think about how these proposals would work.

"Two important areas in which we were unable to include proposals at this point were payroll tax deposit reform and simplification of the earned income tax credit. Simplification is seriously needed in both areas —no doubt about it. . . . We will want to take a further look at these and other proposals as the tax simplification bill advances through the legislative process."

Everyone agrees that our tax system is too complicated. Getting everyone to agree on how to simplify matters can be complicated too, but the consensus we've attained so far shows the potential for real progress. ■

Corporate Tax Burden from page 1

The 1991 overall corporate tax burden, representing a whopping 87 percent of corporate profits, is huge by historic standards. Federal deficit pressure and the sharp growth trend in state/local and payroll taxes can easily push this burden even higher.

"The decade began on a favorable note for corporate America when Congress enacted the Economic Recovery Tax Act of 1981 (ERTA)," according to the study. "If this sizeable tax cut had been allowed to take effect fully over the next several years, it would have substantially reduced overall corporate income tax liabilities. Instead, subsequent tax bills negated the effects of ERTA, and government's drive for more revenue became the major motivation behind most of the far-reaching tax legislation of the decade, with hardly a consideration of sound tax policy."

The cumulative effect of all this legislation was a substantial shift of income taxes from individuals to corporations. "In 1991 alone ... individual income tax receipts will be $291 billion lower than they would have been had the tax code remained unchanged throughout the decade. Corporate income taxes, on the other hand, will be $48 billion higher."

The claim is often made that corporations do not carry their fair share of the tax load, and the statistics accompanying these charges usually show corporate income taxes as a percentage of GNP or federal tax receipts. But when looking at corporate taxes, federal corporate income taxes are only part of the picture.

They have risen 24 percent since 1980, but state and local corporate income tax revenues have increased 39 percent in that time. The largest portion of the business tax burden, however, has become the corporate share of payroll taxes, far outstripping corporate income taxes and currently costing an estimated $153 billion. ■

Mark Your Calendars
November 20, 1991
for the
Tax Foundation's
54th Annual Dinner &
43rd National Conference
at the Waldorf-Astoria
in
New York City

Luxury Tax Misses the Boat As Tax Burden Shifts From Wealthy to Middle Class and Revenue Estimates in Doubt

by Monica Fekete

Last fall, Congress and the President attempted to make the nation's second largest tax increase more palatable to the middle class by adding "progressive" excises, i.e., "luxury taxes" on items which only wealthy people buy. Yachts, furs, automobiles, jewelry, and personal aircraft above a certain price have been subject to a 10 percent excise since January 1, 1991 (see table 1).

For two important reasons this new tax is shaping up to be a failure. First, passing such a narrowly based excise is simply bad tax policy, and second, the impact of the tax has been felt not just by wealthy consumers but by middle class employees in the targeted industries.

Inequitable Tax Policy

An equitable tax should be broadly based, allowing a lower rate and more equivalent effect across industries and income groups. Yet lawmakers negotiating 1990's budget package limited the luxury tax to five industries, and further narrowed their sights to those items with high retail prices.

Lower sales and a host of other negative results can flow from this. But when taxwriters are looking for a quick revenue fix or, as in this case, a highly visible tax on an unpopular group, they often turn to these ineffective "rifle shot" taxes on specific industries or income groups.

Luxury Taxes and the Middle Class

The luxury taxes were enacted under the assumption that they would be paid by the wealthy, but based on preliminary data, sales of luxury items are down, leading to lost jobs in the targeted industries. The revenues collected in the name of the luxury taxes are certainly paid by the wealthy, but middle class workers who lose jobs in the targeted industries can take little solace in that.

Table 1
Luxury Tax Schedule

Item	When Applied	Doesn't Apply When	Tax Avoidance Examples
Jewelry	New or re-worked jewelry over a final value of $10,000, including watches	Repairs and minor modifications	Reworking described as repairs and minor modifications
Furs	New garments made up of at least 25% fur, over a retail price of $10,000	Fur comprises less than 25% of the garment	Bring to the U.S. from Canada, avoiding the taxes since trade between the two countries is tax-free under the new trade agreement
Automobiles	New passenger vehicles over $30,000, counting modifications made within 6 mos. of purchase	Used in business	Wait 6 mos. before making modifications
Boats and Yachts	New boats and yachts over a retail price of $100,000	Used in business unless for entertainment	Purchase overseas and slip in the Bahamas or purchase used
Personal Aircraft	New aircraft over a retail price of $250,000	Used more than 80% of the time for business	Purchase used

Source: Tax Foundation

Revenue Gainer or Loser?

The Joint Committee on Taxation (JCT) estimated last fall that luxury taxes would bring in $25 million in 1991 and $1.5 billion over five years (see table 2). According to the Internal Revenue Service (IRS), the federal government had already collected $33 million in first-quarter taxes as of May 31. The actual tax revenue has exceeded estimates in four of the five industries, with revenue six times higher in the automobile industry and eight times higher for jewelry.

But both the original JCT estimate and the annualized IRS collections ignore the impact of the tax on employees in these industries. When lower potential tax revenues from payroll and personal income tax sources are considered, a net government revenue loss is quite likely.

Other possible implications of the tax include:

- Revenue lost from other sales taxes;
- The high cost of compliance with the luxury tax, both for business and the IRS (the IRS lists on its Form 720 the average amount of time suggested for record-keeping and form preparation for the luxury tax: 2 and 1/2 days per quarter for the average corporation); and
- less corporate income tax revenue due to reduced sales.

Table 2
Estimated Revenues v. Actual Revenues
($Thousands)

Item	Original 1991 Estimate[a]	1991 Revenue Projection from Actual Collections[b]	1st Quarter Actual Collections[c]
Jewelry	$1,000	$8,848	$2,212
Furs	*	1,028	257
Automobiles	20,000	117,032	29,258
Boats & Yachts	3,000	3,600	900
Planes	1,000	480	120
Total	$25,000	$130,988	$32,747

[a] Joint Committee on Taxation.
[b] Annualized IRS collections.
[c] IRS collections data through 5/31/91.
* not available

Conclusion

An efficient and equitable tax should be broadly based — not limited to a specific industry or income group. Unfortunately, the luxury tax does not meet these fundamental criteria for sound tax policy since it targets only five industries and upper income groups.

Although revenue collections have been many times higher than JCT estimates, the tax may in fact lose billions when the full impact on the economy is examined, taking into account compliance costs, lost sales and jobs, and lower income and payroll tax receipts. ■

VIEWPOINT

Top Corporate Executives Bring Concerns About U.S. Competitiveness Before Ways and Means Committee

Lowest Corporate Tax Rate Is Best Government Policy

Allen F. Jacobson

I represent the Emergency Committee for American Trade—better known as ECAT—whose members are the heads of 62 U.S.-based international business enterprises. The annual worldwide sales of ECAT companies are over one trillion dollars, and our companies employ more than five million people.

I also represent 3M—a multinational, multiproduct, multitechnology, multimarket company—which has facilities in over 53 countries. 3M sales in 1990 were over $13.02 billion. Almost 49 percent of those sales were derived from our international operations compared to 37 percent in 1985.

A major accomplishment of our government was the enactment of the Tax Reform Act of 1986 which lowered the corporate tax rate. I can tell you that the lowering of the corporate tax rate has enhanced 3M's competitiveness in the United States and in markets outside our country.

When 3M looks at an investment in equipment, in efficiency or in expansion, it looks at the stream of earnings that the investment will produce. The lower the tax rate, the better the stream of earnings and the more that we can invest and the more we can be competitive. That low tax rate

I can tell you that the lowering of the corporate tax rate has enhanced 3M's competitiveness in the United States and in markets outside our country.

encourages better business decisions and better investment in competitiveness for 3M than tax incentives such as investment tax credits.

In the near future, ECAT will complete and release a study which uses U.S. government data on exports and repatriated earnings of multinational corporations during the 1980s. This study reveals that these U.S.-based multinational corporations made a net positive contribution to the U.S. balance of payments that averaged over $80 billion annually during the period 1980-88.

Something obviously has been going right. What should be done in the future?

I have mentioned the necessity of keeping the corporate tax rate as low as possible. I also think that there is an argument for keeping changes in the tax code at a minimum. The tax system needs a settling down—an extended period of time in which there is no abrupt change in revenue policy. This will serve to improve business planning and performance.

As it looks at the competitive position of the United States in the world economy, the Congress also should be wary of imposing substantial new social costs on business. In 3M's U.S.

As it looks at the competitive position of the United States in the world economy, the Congress also should be wary of imposing substantial new social costs on business.

operations, such costs have been increasing substantially over the years. Right now, our benefit costs are equal to 36.3 percent of our payroll. We believe in giving our employees good benefits, but we ask that you not transfer to us the costs of benefits of other employers.

Many of our ECAT members are concerned about changes that have taken place in recent years to the foreign tax credit and deferral. These changes have been enacted because of a need to increase revenue, but, for many of our members, the amounts of increased tax are not inconsequential and have a negative impact on their competitiveness.

I think that the competitiveness of the U.S. should be foremost in our minds as we consider tax, trade and foreign investment policies and regulations.

We should be careful not to adopt counterproductive policies in our zeal to address balance of trade problems and the national deficit. In the future, as we review the range of challenges faced by the United States as it participates in an enlarged world economy, it may be necessary to remind ourselves that companies cannot be competitive unless they also are profitable. ■

Allen F. Jacobson is Chairman and CEO of 3M Corporation.

Improved Education Needed to Compete

James J. Renier

Honeywell is a stronger international competitor today as a result of fundamental restructuring of the tax code that began in 1986. But we are concerned about the strength of American industry in general.

Global competitors like Honeywell depend on at least five leverage points: cost of capital, productivity, scale of production, global distribution and technology. Our ability to com-

James J. Renier is chairman and CEO of Honeywell Inc.

VIEWPOINT

pete in terms of capital and production relies heavily on our ability to take a long-term view of the development, protection and utilization of technology.

America is still a world leader in computer-aided engineering, artificial intelligence, software engineering, and computer-integrated manufacturing. Utilized effectively, these and other technologies can produce competitive gains. That requires skilled people who can work in this high-tech environment.

Today's jobs require a median of 12.5 years of education. But jobs created during this decade will require 13.5 years, and by the year 2000 a third of all jobs will require a college degree. The ad hoc solutions we have developed in response to the deficiency in our workforce's education is totally inadequate, and the data—with few exceptions—bear this out. What concerns me is that we seem to be reacting to changes in technological competition in a similar ad hoc fashion.

Long-term, risky and expensive investments in technology development are made on the assumption that, if successful, investors will enjoy a long-term return on the investment, and build on its initial success. But sizeable investments can be jeopardized by patent infringements. They have cost our company many millions of dollars, so we place a premium on establishing effective, enforceable intellectual property rules through the Uruguay Round and other trade negotiations. It is important, however, that the negotiations not result in weaker protection than now provided by U.S. trade law.

Development of technology cannot be turned off and on like a faucet. It requires a long-term commitment. For example, Honeywell began R&D on the Ring Laser Gyro—a gyro for aircraft navigation that uses laser beams instead of moving parts—in 1962. It has since become the standard of the industry, worldwide, but it did not become profitable until 1985.

Like the utilization and protection of technology, advances in the state of the art will not happen automatically. Industry must see the potential gain in the enterprise, and must be confident that Congress understands and considers industry needs. ■

High-Tech Success Vital to U.S. Economy

James R. Houghton

I am very troubled about American competitiveness. One must be alarmed when:

- seven of the top ten recipients of U.S. patents are foreign companies;
- U.S. industry is weak or losing badly in one-third of the critical generic technologies that drive economic prosperity; and
- the U.S. world market share in data processing and office automation equipment—the very tools of the Information Age pioneered in the United States—has dropped from 51 percent to 32 percent since 1984.

But rather than focusing on the negative, I'd like to urge:

- a commitment to technology;
- a long-term business orientation; and
- a commitment to total quality.

As Corning learned with the success of fiber optics, we can't create good paying jobs for our workers unless we invent new products and new processes.

So what can government do? I commend a technology plan for governmental action developed by the Council on Competitiveness, whose recommendations include:

There are policy levers that can be used to reduce the cost of equity, thus encouraging firms to be more long-term oriented . . . [such as] reducing the federal budget deficit or by creating incentive for private savings.

- making research on generic industrial technologies a national R&D priority as stated in the President's proposal;
- creating an economic climate more conducive to manufacturing, innovation, and investment in technology by such measures as the permanent extension of the R&D tax credit;
- communicating the priority of technology and competitiveness to the American public as President Kennedy did after Sputnik; and
- developing policies and programs to ensure that we have a world-class technology infrastructure, including an improved educational system.

U.S. businesses need to be more long-term oriented. Unfortunately, the financial pressures on American business managers are for short-term results. I'm convinced that our short-term orientation is driven by our relatively high cost of capital, particularly the cost of equity.

The cost of capital is composed of two parts: the cost of debt and the cost of equity. Our cost of debt—interest rates—is similar to that of our principal technology competitors, Japan and Germany. But most economists agree that our cost of equity—the return our shareholders expect—is substantially higher. One study indicates that it is as much as 4 to 6 percentage points higher.

There are policy levers that can be used to reduce the cost of equity, thus encouraging firms to be more long-term oriented. One is increasing the pool of savings which finances most equity investments. This could be achieved by reducing the federal budget deficit or by creating incentive for private savings. Another possible solution is encouraging equity investors to be more long-term oriented by allowing a lower tax on capital gains after an extended holding period.

I realize that technology and long-term orientation alone won't make America competitive, but progress in these areas is a vital component of a strategy for American competitiveness. ■

James R. Houghton is Chairman of the Board and CEO of Corning Incorporated.

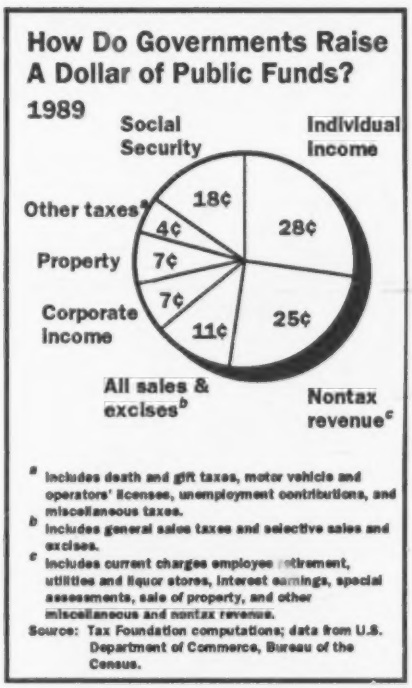
How Governments Raise and Spend Each Dollar of Public Funds

How Governments Collect . . .

Just over 28 cents of every dollar raised by federal, state, and local governments came from individual income taxes during fiscal year 1989, according to Tax Foundation analysis of the latest reported data. Over the course of several years, the individual income tax had been slowly losing its dominance as governments' principal revenue source. But this trend was reversed in 1989, as governments tapped that source for 28.3 percent of their revenue, up from 27.6 percent in 1988. Individual income taxes accounted for 40 percent of all federal revenues, but for states it was only 15 percent, and it constituted a mere 1.7 percent share for local governments. In the aggregate, the individual income tax raked in $543 billion of the total $1.917 trillion in revenue received by all levels of government combined.

Other High Revenue Sources

The federal Social Security program was FY89's second largest government revenue source, netting 18 cents of each tax dollar collected, or a total of $339.5 billion. These payroll taxes, which are collected by neither state nor local governments — only by the federal government, have nevertheless been the fastest growing of all taxes over the last three decades. In 1989 Social Security tax collections were 30 times as large as in 1960, rising from 7 cents per dollar of total government revenue to 17.7 cents.



[a] Includes death and gift taxes, motor vehicle and operators' licenses, unemployment contributions, and miscellaneous taxes.
[b] Includes general sales taxes and selective sales and excises.
[c] Includes current charges employee retirement, utilities and liquor stores, interest earnings, special assessments, sale of property, and other miscellaneous and nontax revenue.
Source: Tax Foundation computations; data from U.S. Department of Commerce, Bureau of the Census.

Sales Tax Contributions Falling

Despite rising from $16.9 billion in 1960 to $105.5 billion in 1989, government collection of selected sales and excise taxes has declined in relation to the growth of other taxes. Gasoline, tobacco, and alcohol excises are the principal taxes in this category, and as a portion of each tax dollar collected, they have declined from 12.5 to 5.5 cents over the thirty-year period.

Government Deficits

Despite government collections $141 billion higher in 1989 than in 1988, total government deficits declined only $30.8 billion to $113.2 billion, thanks to a rise in total spending of $110 billion. The federal government's deficit alone was $177 billion, or 14 percent of federal outlays. State and local governments bailed out the federal government to some extent by producing surpluses of $62 billion and $1.5 billion respectively. (See table 1 for details.)

See Taxing and Spending on page 7

Table 1

How Federal, State, and Local Governments Raise Each Dollar of Public Funds

Selected Fiscal Years 1960-1989

(Cents Per Dollar of Total Revenue)

Source	1960	1970	1980	1988	1989
Total Tax Revenues	82.7	82.4	78.2	74.9	75.5
Individual income	28.2	30.3	30.7	27.6	28.3
Social Security (OASDHI)	7.0	11.5	15.0	17.5	17.7
Property	10.7	10.2	7.3	7.4	7.4
Selective sales & excises	12.5	9.8	6.5	5.8	5.5
Corporate income	14.8	11.0	8.4	6.6	6.7
General sales	3.5	4.8	5.5	5.9	5.9
Other taxes [a]	6.0	4.8	4.8	4.0	3.9
Nontax Revenues	17.3	17.6	21.8	25.1	24.5
Current charges	8.1	7.9	8.6	9.8	9.4
Miscellaneous general [b]	3.3	4.0	6.7	7.1	7.0
Employee retirement	1.9	2.5	3.1	4.6	4.5
Utilities and liquor stores	3.2	2.6	2.7	3.0	2.9
Other Nontaxes	0.8	0.6	0.7	0.6	0.7
Exhibit ($billions)					
Total revenues	$153.1	$333.8	$932.2	$1,776.0	$1,917.5
Surplus or deficit (-)	$1.8	$0.8	-$26.5	-$144.1	-$113.2

[a] Includes death and gift taxes, motor vehicle and operators' licenses, unemployment contributions, and miscellaneous taxes.
[b] Includes interest earnings, special assessments, sale of property, and other general revenue.
Source: Tax Foundation computations based on data from U.S. Department of Commerce, Bureau of the Census.

Table 2

How Federal, State and Local Governments Spend Each Dollar of Public Funds

Selected Fiscal Years 1960-1989

(Cents Per Dollar of Total Spending)

Source	1960	1970	1980	1988	1989
Major social welfare programs, total	20.1	25.5	33.2	31.7	30.1
Social Security (OASDHI)	7.1	10.8	15.6	15.6	15.8
Social services and income maintenance [a]	11.0	12.3	14.5	12.9	11.1
Government employee retirement	2.0	2.4	3.1	3.2	3.2
National defense and international relations	32.3	25.3	15.6	17.2	17.1
Education	12.8	16.7	15.0	13.4	13.8
Interest on general debt	6.2	5.5	7.9	10.5	10.9
Environment and housing	5.4	4.4	5.0	6.7	5.3
Utilities and liquor stores	3.4	2.8	3.8	3.6	3.6
Transportation	7.6	6.2	4.5	3.7	3.7
Public safety	1.8	2.0	2.3	3.5	3.6
Government administration	1.8	1.9	2.2	2.5	2.6
Postal service (Federal)	2.5	2.3	1.9	1.8	1.8
Sanitation	1.1	1.0	1.4	1.2	1.3
All other	5.0	6.4	7.2	4.2	6.2
Exhibit ($Billions)					
Total spending	$151.3	$330.0	$958.7	$1,920.1	$2,030.7

[a] Includes public welfare, hospitals, health, social insurance administration, veterans benefits, and other insurance trust expenditures.
Source: Tax Foundation computations based on data from U.S. Department of Commerce, Bureau of the Census.

Taxing and Spending from page 6

. . . And How They Spend

Social Welfare Programs Continue to Dominate

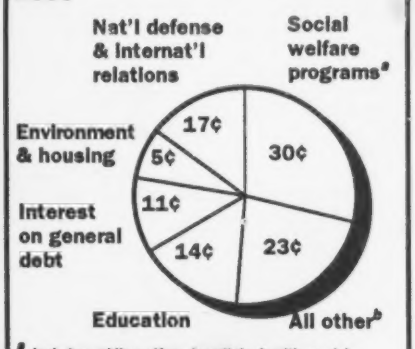
Governments spent $612 billion on social welfare programs in 1989 (latest reported data), over 30 cents of each dollar governments spent. Federal Social Security accounted for half of social welfare expenses, or 15.8 cents of every government dollar. Also included in this category are such social services and income maintenance programs as public welfare, health and hospitals, veterans benefits, and unemployment insurance. These accounted for 11 cents of each dollar of government spending. Another substantial component of social welfare programs is government employee retirement, which took 3 cents of every dollar in 1989 (see table 2 on page 6 for details). Although spending on social welfare expenditures increased $44.3 billion from 1988 to 1989, this category actually received a smaller piece of the ever-larger spending pie, 30.1 cents per dollar instead of 31.6.

The same is true for national defense and international relations, which despite a spending increase of $16.3 billion from 1988 to 1989, actually constituted only 17.1 cents per dollar spent in 1989 instead of the 17.2 cents it represented in 1988. Over the last thirty years, social welfare expenditures have appropriated more and more government spending, mostly at the expense of national defense. A comparison of 1960 spending figures with 1989's shows a virtual flip-flop of the two categories, with social welfare spending increasing from 20.1 to 30.1 cents per dollar while national defense and international relations dropped from 32.3 to 17.1 cents. As health and retirement costs soar and the government announces new military cutbacks, this trend seems likely to continue.

The fastest growing of all government costs has been debt-related outlays. Interest payments on government debt were 6.2 cents in 1960, 7.9 cents in 1980, and 10.9 cents in 1989 when the nation spent nearly $221 billion dollars on maintenance of prior debt. Most of this interest cost was due to the federal debt, which reached $2.88 trillion in 1989. State and local governments have much less debt ($798 billion aggregate) due to constitutional and legislative requirements mandating balanced budgets. ■

How Do Governments Spend A Dollar of Public Funds?

1989



[a] Includes public welfare, hospitals, health, social insurance administration, veterans benefits, and other insurance trust expenditures.

[b] Transportation, utilities and liquor stores, public safety, government administration, postal service, sanitation, and all other.

Source: Tax Foundation computations; data from U.S. Department of Commerce, Bureau of the Census.

FOUNDATION MESSAGE

Tax Action Moves From Nation's Capital to State Capitals

Dan Witt
Executive Director

When the federal government's taxwriting machine heats up, Washington, D.C. is the best seat in the house — for lobbyists, for policy analysts, for any citizens concerned about government taxing and spending. But in 1991 Washington insiders are looking wistfully past the beltway — it's the year of the states. California and New York have already passed major tax bills, and together with Pennsylvania, Connecticut and Texas, where action is still pending in legislative sessions, the combined tax increases at the state level this year will exceed the gigantic federal tax increase passed in 1990.

What is the cause of this flurry of taxwriting in state capitals? 'Recession' is the most commonly heard answer. And it's true that the recession has made a mockery of state revenue estimates. It has devastated sales tax revenues and, with employment flagging, states have suffered the double-whammy of lower payroll tax revenue and higher unemployment compensation. It is definitely the proximate cause of the huge state budget deficits we are seeing.

On the other hand, we have just finished a decade of steady economic growth with GNP rising an average of 7.4 percent. Did state coffers grow to the point where they could withstand a recession? Just the opposite. State spending increased an average of 8.5 percent per year, and state/local debt grew an average of 8.2 percent annually during the decade. And this pattern of accelerating state/local taxes is not a phenomenon of the 1980s; since 1950, state/local taxes have increased from 6.10 percent of GNP to 10.75 percent.

The net result is that states in bad fiscal shape are raising taxes. Will they do so in a way that minimizes negative impact on the economy? Or will they go on a desperate revenue-raising spree with no thought to sound tax policy?

Unwilling to pass judgment long-distance on state fiscal problems, the Tax Foundation is holding a series of programs in the states to answer these questions. The general theme will be "Tax Policy and Economic Growth," and each program will feature state-level government officials, as well as authorities from local universities and major corporations in the area.

The next issue of *Tax Features* will report on our program in Chicago July 24th and preview our upcoming seminar in Pittsburgh. State tax issues are even harder to track than federal developments, so stay tuned.

Foundation's Policy Council Holds Tax Policy Colloquium in NYC

The Foundation's Policy Council and distinguished guests convened June 19 in the offices of the Metropolitan Life Insurance Company in New York City. Hosted by Stuart Nagler, senior executive vice president at Met Life, the luncheon was an off-the-record roundtable on current issues in tax policy. Corporate executives and university scholars discussed such issues as tax "fairness," and the revenue estimating process.

Robert Bartley, Editor, Wall Street Journal

Senator Harry F. Byrd, Jr., recipient of the Foundation's Distinguished Service Award.

James Q. Riordan, co-chairman of the Tax Foundation.

University of Texas Law School Student Finishes Internship at Foundation

Monica Fekete is finishing her term as the Foundation's summer intern and returning to Austin, Texas to continue her legal education. The Foundation offers internships every summer as an extension of its College Classroom Project. Ms. Fekete reported on congressional testimony and conducted studies of government taxing and spending, the current status of the government's indebtedness, and the newly passed luxury tax (see page 3). ■

◀ *Monica Fekete pictured with Gregory Leong (l), Director of Special Studies, and Paul Merski, Director of Fiscal Affairs.*

Tax Features

Tax Features (ISSN 0883-1335) is published by the Tax Foundation, an independent 501(c)(3) organization chartered in the District of Columbia. Original material is not copyrighted and may be reproduced. Please credit Tax Foundation.

Co-Chairman ..... James Q. Riordan
Co-Chairman ..... James C. Miller III
Executive Director ..... Dan Witt
Director of Fiscal Affairs ..... Paul G. Merski
Senior Fellow ..... B. Anthony Billings
Editor ..... William Ahern
Editorial Asst. ..... Gretchen Georgiadis
Director of Special Studies .... Gregory Leong
Tax Analyst ..... Monica Fekete

Tax Foundation
470 L'Enfant Plaza, S.W.
Suite 7400
Washington, D.C. 20024
202-863-5471

Tax Foundation
470 L'Enfant Plaza, S.W.
Suite 7400
Washington, DC 20024

Non-profit Org.
U.S. Postage
PAID
Washington, DC
Permit No. 5229

Sir or Madam
Congressional Info. Service
SRI
4520 East West Highway
Bethesda, MD 20814